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## **The Tax Shuffle**

### **Mayor Eddie Perez Has A Proposal To Fix The State's Tax System, And This Time The Legislature May Actually Be Open To His Ideas**

By Meir Rinde

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With the advent of the new political year, Mayor Eddie Perez has come out with his legislative agenda — not only for the city but for the state, which, after all, pays for almost half of the city's \$470 million annual budget.

For next year, he wants the legislature to increase funding for Hartford's schools and general government by another \$15.5 million.

He wants the state to take on debt to upgrade the city's flood control system, to build a new police headquarters near downtown, to repair housing projects and to rehab parks.

And he wants legislators to make big, expensive changes in the tax code, in part by creating a new income tax credit for local property taxes.

If you own a home in Hartford, New Haven, or any of the state's poorest cities and towns, the proposal would let you reduce your state income tax bill by up to \$3,500, depending on how much you paid in city property taxes. The goal is to promote homeownership in the interest of stabilizing neighborhoods. Residents could also take a credit for car taxes.

"This is clearly a boon to homeowners and people who own cars, which includes renters," said Matt Hennessy, Perez's chief of staff. "It's clearly a middle-class benefit."

If approved by the General Assembly, the plan would constitute a major change in the state's tax system.

It's not the first time Perez has suggested ambitious tax plans, but his previous efforts have died in the legislature. The last time that happened was last year, when he proposed the unprecedented idea of limiting a homeowner's property taxes to four percent of his income. The plan would have turned the property tax into a sort of hybrid income tax, and it never had a chance.

But this time, the plan is for all of Connecticut, not just Hartford. And rather than just seeking to blunt the effect of residents' rising tax bills, it has the much more ambitious aim of addressing fundamental flaws in the way the state raises money to pay for education and other services, flaws that lawmakers have complained about for years but haven't had the will to fix. Unlike last year, Perez and the legislature seem finally be on the same page. For the first time, his tax plan might actually have a chance at

success.

"The approach of using a tax credit on the income tax has already gained widespread acceptance in the legislature," said New Haven Mayor John Destefano, who made tax reform central to his recent gubernatorial campaign. "They're familiar with it. Look, property taxes are an issue all over the state. It's not just an urban issue. So it's going to get attention."

Perez's first attempt at tax reform was in 2004, when he hatched the idea of a homestead exemption. It would have cut tax bills for homeowners by taxing them as if their houses were worth much less than their assessed value. The idea had some support, but it would have paid for itself with a jump in taxes for business taxpayers and landlords (and, via rent increases, their tenants). The business lobby fought it hard, and the plan died.

"There's been so much disagreement on it," House Speaker Moira Lyons told the *Hartford Courant*. "It's had so many problems." Instead, the legislature allowed Hartford to delay its required property revaluation for two years, leaving tax bills basically unchanged.

Last year, with the delay set to expire, Perez tried a different track, proposing the four-percent-of-income limit. Having learned he needed business on his side, he also proposed getting rid of Hartford's special 15 percent tax surcharge on commercial properties. Homeowners would get a break, businesses would get a break, and only landlords and renters would be screwed. But the plan was so nuts that the business lobby rebelled again, despite the potential benefits it would reap.

Perez seemed a little nuts, too: when the proposal was still stalled in April, just before the end of the legislative session, he sent out an e-mail proclaiming imminent catastrophe. Revaluation would double residents' tax bills, he'd have to cut millions from the city budget to keep taxes down, and he'd have to close schools and fire cops. "We are days away from the city being forced to prepare to deeply slash city services," he claimed.

Legislators were annoyed that the mayor was trying to tell them what to do. "It's a form of bullying," House Minority Leader Robert Ward said.

Once again, Perez's plan died.

Instead, the legislature simply eliminated the business surcharge and allowed a phased-in revaluation, limiting residential property tax increases to 3.5 percent per year.

In some ways, the new plan resembles the old plans. Once again, it targets homeowners. It would let them reduce their state income tax bill by the amount of local property taxes they paid, up to a limit. All homeowners would take up to \$1,500 off their annual income tax bills. In poor cities — those where less than half the people own their homes, like Hartford and New Haven — they could take a tax credit of up to \$3,500. In either case, you could cut your income tax bill by up to 75 percent.

Once again, the plan is tied to income, though this time it could actually benefit wealthier people who live in poor cities. Consider the homeowner who has a \$3,500 property tax bill. If his state income tax bill comes to \$5,000, he can take the full \$3,500 credit. But if he's not such a big earner, and he only owes the state \$2,000, he can only take a credit of \$1,500, because of the 75 percent limit.

Once again, landlords and renters would be screwed, though a Perez spokeswoman said the plan allows non-homeowners to take a credit for their car taxes. (Separately, Perez also advocates creating a state version of the Earned Income Credit, which can give poor families a refund bigger than their tax bill, putting cash in their pockets.)

The new element is that the plan would help shift the way the whole state pays for education and other services. By giving an income tax credit for property taxes, the plan would subsidize property taxes; the state would essentially be giving more money to cities. It's a way of reducing their reliance on property taxes, and in that way Perez has invited political support for the plan from a new constituency — the legislators and local officials who have complained for years about property taxes, and the citizens they represent.

The dependence on the property tax, they say, results in a push for constant economic development, which eats up land and promotes sprawl in the name of expanding the tax base. It also divides communities, with young families supporting tax increases to pay for schools and older residents worried about being taxed out of their homes.

Bill Curry, the former state comptroller and gubernatorial nominee, applauded Perez for making a “groundbreaking” proposal. “Eddie once again gets credit for stepping up to the plate on a tough issue,” Curry said.

But along with his praise, Curry offered a number of criticisms. Tax reform should help small businesses more directly, it shouldn't favor big cities over small towns, and it should do more for renters, he said.

“Politically, you need to bring everyone in here,” Curry said. Likewise, Destefano said Perez's proposal by itself does not address some important issues, like the state's Education Cost Sharing formula, which determines how much each town gets for its schools. The legislature may reform that formula this year, and any increase in funding would likely require higher income taxes.

And there's the rub. The new tax credit would cost a lot of money. Hennessy said it would run to “hundreds of millions of dollars,” but it could easily be much higher. Legislative staffers haven't crunched the numbers yet, but here's one way to think about the cost: the state has over 900,000 homeowners, according to the U.S. Census; if each one took an average credit of \$1,500, it would cost the state more than \$1.35 billion.

Even if the state could raise or free-up that much money, many legislators would want to spend it on a new universal healthcare plan, education spending, the underfunded teacher's pension plan or other programs.

In addition, Perez's proposal does not guarantee that property tax rates won't keep going up. For practical and political reasons, state legislators will have to make sure that the strategy they choose isn't simply a formula for higher overall taxes and bigger municipal budgets, Destefano said.

“Controlling state expenditures or capping municipal expenditures, even if it's on an interim basis, has to accompany such a dramatic change,” Destefano said.

Otherwise Hartford and other cities could take the state income tax money and just keep asking for more.

Under Perez's plan, "almost all of the city's tax revenues would come from commercial taxpayers and the state, and a scant amount from residential taxpayers," said Representative Art Feltman, who will run against Perez in this fall's mayoral election. "The implication is that residents would have very little connection and very little concern about what the city spends. Commercial taxpayers don't vote in Hartford, and the state doesn't vote in Hartford, and therefore there would be no check on the city's budget." ●

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